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Economic Intelligence Weekly

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5 June 1974

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Note: Comments and queries regarding this publication are welcomed. [redacted]

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Comparative Indicators

The oil situation is now being covered mainly in *International Oil Developments*, published each Thursday morning.

ECONOMIC INTELLIGENCE WEEKLY

Articles

CANADA: PROVINCIAL TAXES THREATEN MINERALS DEVELOPMENT

Four Canadian provinces, desiring to share more fully in record profits from foreign sales of non-energy minerals, have sharply increased taxes on the mining industry. The new levies already have caused reconsideration of several major investment projects. In time, they could substantially curtail growth of mineral production, much of which goes to the United States.

Provincial tax measures recently adopted or planned:

- British Columbia adopted a minimum tax on mines of 2.5% of sales this year and 5% thereafter, with an additional 50% tax on any income derived from that portion of the selling price exceeding 120% of the average price in the preceding five years.
- Ontario adopted a change in the corporation income tax for mining and other resource development industries from a flat 15% to a graduated levy going as high as 40%; most companies are large and will have to pay close to the maximum rate.
- Manitoba adopted an increase in the royalty rate from 15% to 23%. A proposed law would further increase the rate to 33-1/3% on 1 January 1975 and impose a 50% surcharge similar to that of British Columbia.
- Saskatchewan plans a large property tax on the assets of producers of potash, the province's principal non-energy mineral product.

The four provinces produce two-thirds of Canadian non-energy mineral output, which totaled about $5 billion in 1973. The United States obtains from the provinces more than half of its supplies of nickel and potash and 10%-50% of its tantalum, asbestos, cadmium, zinc, and silver. The threat of higher provincial taxes already has caused the Texas Gulf Corporation to suspend a $95 million expansion of its copper, lead, and zinc mines at Kidd Creek in Ontario and to postpone construction of an associated $120 million copper smelter. Kennecott Copper Company is reconsidering plans for a $450 million copper mine and smelter in British Columbia. Officials of many other mining companies, especially in British Columbia, are complaining loudly. At least another $550 million worth of planned minerals development projects scheduled for completion by 1980 is jeopardized.

The mining industry also faces the possibility of higher federal corporation income taxes. The proposed federal budget for 1974-75, defeat of which brought down the Trudeau government last month, would have reduced mineral depletion allowances and eliminated deductions by mining and petroleum companies for tax and royalty payments to provincial governments. Some form of higher federal tax is almost certain, whichever party gains control in the coming election, set for 8 July. [redacted] 25X1

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OECD MEMBERS SIGN STANDSTILL AGREEMENT

OECD members last week agreed to abstain for one year from using beggar-thy-neighbor policies to deal with their severe payments problems. The agreement means different things to the nations involved, however, and its implementation will entail difficult negotiations in the months ahead. The declaration, while not legally binding, will help members resist growing protectionist pressures.

At the meeting in Paris, OECD members pledged to:

- Avoid unilateral measures to restrict imports and other current account outflows;
- Avoid artificial stimulation of exports, including competitive export credit;
- Avoid export restrictions contrary to the objectives of the charter;
- Consult with one another on emergency measures under consideration;
- Give due regard to the special needs of developing countries.

The declaration, which provides no mechanism for enforcement, generally leaves interpretation of the provisions to individual countries. Italy and Denmark will be allowed to maintain the unilateral trade restrictions adopted in recent weeks, having promised to moderate the measures when their situation improves. Other countries in serious straits, including the United Kingdom, Greece, and New Zealand, apparently believe the declaration permits actions to correct persistent non-oil deficits.

The wording on the ban on export restrictions had to be particularly loose to satisfy all parties. Natural resource exporters -- such as Canada, the Nordic countries, and Australia -- were reluctant to accept a ban. They feared that a sudden rise in export orders could further disrupt their economies. Natural resource importers, e.g. Japan and the European Community, were determined that a ban should be included. These countries feared stringencies in key imported raw materials.

If the present accord is to be more than a pious hope, the more prosperous OEDC nations will have to adopt cooperative lending policies and the nations in trouble will have to introduce austerity measures. The burden of cooperative financing will fall mainly on West Germany and the United States.

Bonn is willing to grant credits to EC member states in balance-of-payments difficulties only if they undertake effective stabilization programs. But, the new governments of Italy and the United Kingdom may not be politically able to put their economic houses in order. These two countries alone are expected to accumulate current account deficits totaling $18 billion this year. Bonn is sufficiently alarmed about Italy's plight to consider participating in a large loan, provided that Rome puts up part of its gold reserves as collateral. [redacted] 25X1

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CHINA STEPS UP INTEREST IN GRAIN IMPORTS

Since mid-May the PRC has taken measures to speed up grain deliveries and has re-entered the grain market as a buyer.

- Peking has discussed the problem of TCK smut in US wheat with a team of USDA and grain trade experts. Chances now appear good that deliveries of US wheat will soon be resumed.

- China has resumed chartering of vessels to load US corn. In April the PRC abruptly withdrew eight vessels from this trade, ostensibly because of port congestion in China.

- The PRC recently signed contracts for 250,000 tons of wheat and 500,000 tons of corn from Argentina and for upwards of 400,000 tons of French wheat.

- A Canadian delegation recently arrived in Peking to negotiate the price of wheat for July-December delivery.

The much publicized dispute over TCK threatened a complete breakdown in deliveries of US wheat to China. The issue reflected a legitimate concern over the introduction of a new wheat disease into China. The dispute also provided a convenient opportunity to delay deliveries because of congestion in North China's ports. The Chinese now insist that the grain be delivered, rejecting offers by the traders to cancel the balance of the contracts. USDA has proposed tighter US inspection standards in return for a Chinese promise that no cargoes will be rejected upon arrival in China. The USDA may well have difficulty selling this plan to all US shippers of wheat because of the higher costs of meeting these standards.

China probably will import more than the 8.8 million tons of grain already contracted for delivery in 1974. Crops have been set back by drought in the north and by drought and unseasonable frost in the south. One high-level Chinese government official reportedly said the winter wheat crop this year will be less than the 1973 crop. The erratic behavior of the monsoons is forcing shifts in planting schedules that will lower yields of fall-harvested crops. [redacted]

Purchases of Grain for Delivery in 1974

Thousand Tons

Source	Wheat	Corn	Total
Total	**5,940**	**2,900**	**8,840**
United States	2,100	1,900	4,000
Canada	2,000	0	2,000
Australia	1,200	0	1,200
Argentina	250	1,000	1,250
France	390	0	390

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US CARGO PREFERENCE LAW WORRIES EUROPEANS

Norway and other West European shipping nations are concerned about proposed US legislation that would reserve 20% of US oil imports for US tankers. If passed, the legislation would constitute the first across-the-board US cargo preference statute affecting commercial as opposed to government-controlled cargoes. Until now only two categories of commercial cargo have been reserved for US ships: the US/Soviet Maritime Agreement guarantees that the ships of each party shall have the opportunity to carry one-third of US/Soviet trade; and a pooling agreement (sanctioned by the Federal Maritime Commission) between US and Brazilian steamship companies allocates 40% shares of liner cargo in US/Brazilian trade to ships of those countries. Under Public Law 480 and similar legislation, 50% of US aid cargoes and US Government-financed cargoes must be carried in US-flag vessels.

With the major exception of France, which reserves half of its oil imports for French tankers, non-Communist industrial countries have no cargo preference legislation on the books. The strongest support for this concept comes from the developing countries of Latin America, at least 10 of which have laws reserving cargoes for ships under their national flags. Two Asian developing countries with similar laws are Sri Lanka and Thailand. The USSR and other Communist governments have less need for cargo preference laws. Their trading organizations select the carriers for all f.o.b. imports and all c.i.f. exports.

Countries whose ships are most active in carrying liner and tramp cargoes outside their home country trade are most vulnerable to cargo preference laws. These include the United Kingdom, Norway, Sweden, Denmark, the Netherlands, and Greece. American, Greek, and overseas Chinese firms owning sizable tonnages of tramp vessels under the Liberian and other flags of convenience are in a similar situation. [redacted]

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KAISER MAY BUILD SOVIET ALUMINUM PLANTS

Kaiser Industries has taken another major step toward helping the USSR boost its aluminum capacity by signing a protocol with the Soviet Ministry of Nonferrous Metallurgy.

Discussions have centered on the construction of a 1 million-ton alumina refinery, a 500,000-ton aluminum reduction plant, and a large rolling mill. Kaiser officials estimate that $1.4 billion in Western equipment will be required for the three plants. Tough negotiations lie ahead, especially over financing and the price and volume of Soviet aluminum to be sold to Kaiser in repayment. Nonetheless, both Kaiser and Soviet officials appear optimistic about reaching final agreement.

The Soviets are also negotiating with France's Pechiney Ugine Kuhlmann for a billion dollar deal involving the construction of a second 500,000-ton aluminum reduction plant and another alumina refinery. The Kaiser and Pechiney projects figure strongly in Soviet plans to expand aluminum output in 1976-80. With combined capacities of 1 million tons per year, these projects would increase Soviet production by about 50%.

The two projects would have little effect on world bauxite markets. The Kaiser project will utilize domestic nepheline ores from the Kola Peninsula and the French project will be tied to a large Soviet-financed bauxite project nearing completion in Guinea. The completion of the plants could have a significant effect on world aluminum markets, however, because much of the 1 million tons in aluminum to be produced from the two projects probably will be available for export. The Soviets already are major exporters of aluminum – over 500,000 tons in 1973 – and by 1980, if the new plants are completed, could become the world's largest exporters.

Kaiser has already formed an international consortium to assist in the management of its project as well as in the disposition of the aluminum the Soviets will supply in repayment. Kaiser has also arranged the necessary financing from a banking consortium (probably international) headed by Bank of America and the First Boston Corporation. The consortium is willing to provide the necessary financing even if Eximbank funds are not available.

Several problems remain to be resolved before final agreement can be reached. The USSR undoubtedly wants Eximbank participation, which would lower total Soviet interest payments by roughly $100 million while extending considerably the length of the loan. For its part, Kaiser will probably insist that the Soviets supply aluminum under a long-term contract, probably 25 years or longer. Prices of Soviet aluminum, always a sticky issue, have yet to be discussed. If final agreement is obtained, the deal will be the largest concluded to date between the USSR and a US firm. [redacted] 25X1

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TRADE RESTRICTIONS UPSET WORLD BEEF MARKET

Import barriers in the European Community and Japan are diverting increased amounts of foreign beef to the US market, reinforcing downward pressure on prices.

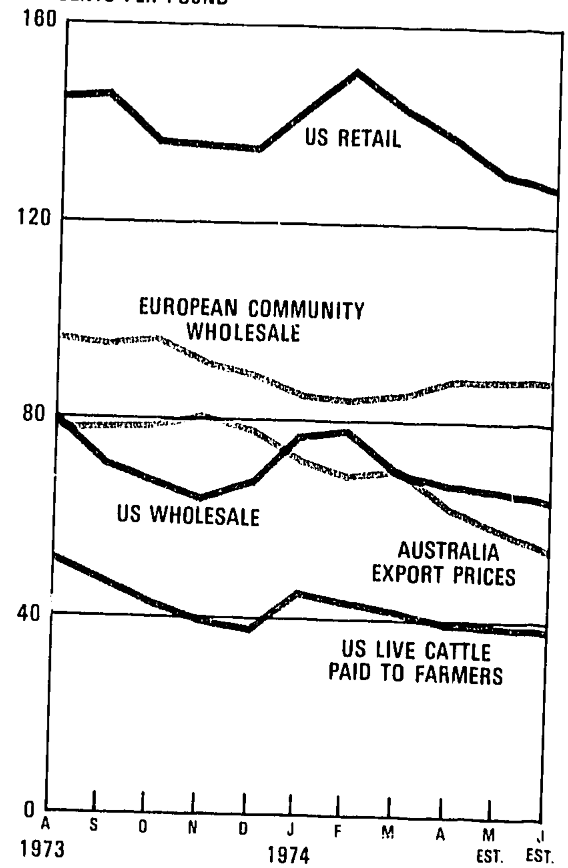
International beef prices have been softening since last August as a result of a dramatic three-year increase in the number of cattle and a leveling off in demand. Total beef production in Free World countries is expected to rise by at least 10% in 1974. At the same time, sluggish growth in real consumer income and resistance to high prices have brought the growth in beef consumption practically to a halt. Prices will have to drop further if consumers are to take up the additional supplies.

In response to falling prices, the EC has imposed numerous import barriers since September to protect domestic producers. Japan suspended beef import licenses from 1 February to the end of 1974. The European actions have caused South American exports to plummet. South American beef is largely barred from the US market for sanitary reasons, but Australia and New Zealand have reacted to EC and Japanese restrictions by raising shipments to the United States.

These trade restrictions threaten to push US prices lower than would be expected merely from the new supply/demand relationship in the Free World. US imports in the first quarter of 1974 were up 6% from the same period last year, and red meat in cold storage on 1 May was at the highest level in 22 years. An 18% increase in US imports is forecast by USDA for 1974, compared with a decrease of 40% for the EC and Japan.

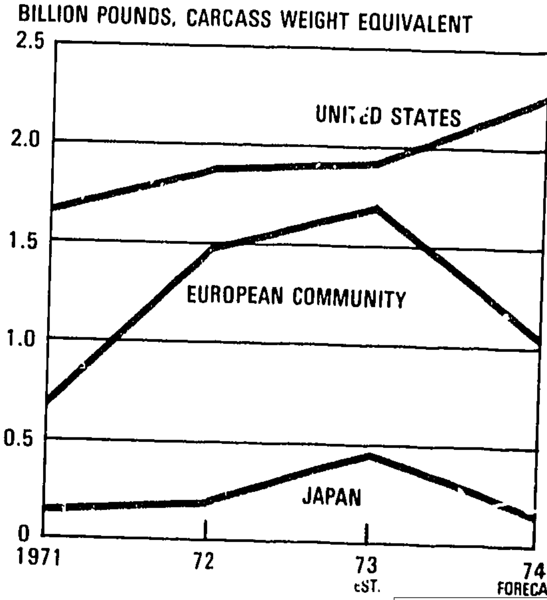
WORLD BEEF PRICES

US CENTS PER POUND



BEEF IMPORTS OF MAJOR IMPORTING COUNTRIES

BILLION POUNDS, CARCASS WEIGHT EQUIVALENT



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World beef production is expected to increase even more rapidly in 1975, especially if feedgrain prices ease from their present high levels. USDA estimates that Free World beef production will increase by 20% in 1975 provided that slaughter rates recover to the average of the 1960s. Production could rise even more if a poor outlook for profits induced producers to reduce herd sizes. The large gain anticipated in output should depress prices further. 25X1

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VENEZUELA: MIXED IRON ORE COMPANIES PLANNED

President Perez has announced that mixed government-private companies will be formed to operate Venezuela's iron ore industry. The two US companies whose concessions are to be nationalized – subsidiaries of US Steel and Bethlehem Steel – will be permitted roles as junior partners. They currently supply about one-third of US iron ore imports.

Compensation negotiations with the companies are in a preliminary phase. Caracas has asked them to submit financial and operating data. Negotiations setting a timetable for taking over the mines in one to three years are to begin in a few months.

The issue of greatest concern to US Steel is continued access to Venezuelan ore. An abrupt loss of this ore would seriously affect the company's operations until alternative sources of supply could be developed. US Steel claims it needs seven years or more to do this. Caracas is willing to allow shipments to continue at least until alternative sources are developed.

Venezuela wants to eliminate iron ore exports and conserve the resource for its own use. Its reserves of about 1.8 billion tons (75 years' output at the present extraction rate) are to be used for its domestic steel industry. Caracas plans to increase annual steel production from the present 1 million tons to as much as 15 million tons, largely for export, by the mid-1980s. Steel production at this level would require approximately the same amount of iron ore as is now produced (about 24 million tons). More than one-half of current production goes to the United States. 25X1

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Notes

Weather Depresses Canada's Wheat Prospects

Heavy rains and cold temperatures have delayed planting in Canada's major wheat-growing regions. Durum already has been hard hit; the inability of many farmers to meet the 31 May planting deadline has forced a diversion of 60% of planned durum acreage to barley and oats. Since Canada usually accounts for 25% to 45% of durum exports, the expected 1.3 million-ton-production drop will have a substantial impact on world durum prices. Unless weather conditions improve within the next week (contrary to forecasts), delays in planting breadwheat as well could hold total Canadian wheat production 15%-20% below the 18.5 million tons previously expected. [redacted] 25X1

New Delhi Overstates Grain Contracts

The public statement by Food Minister Shinde last week that India has recently contracted for 3 million tons of US grain is premature. Firm contracts actually total little more than one million tons. The statement does, however, reflect stepped-up government efforts to import more grain following the poor spring harvest. Imports from all sources may total 5 million tons in 1974, compared with 4.2 million tons in 1973. Official exaggeration of contracts in hand is intended to (1) boost the government's domestic procurement program and (2) stabilize urban markets where wholesale foodgrain prices rose 11% in the first four months of 1974. [redacted] 25X1

Bulgaria Borrows Heavily for Western Equipment

Bulgaria, already saddled with a heavy debt service burden, is preparing for a major buying binge in the West. Breaking its rule of linking credit to specific projects, Sophia recently tapped the Eurodollar market for $95 million in untied loans – one for $50 million orchestrated by the Franklin National Bank of the United States and one for $45 million set up by Crédit Commercial de France. Total borrowing from the West since January now amounts to at least $210 million. [redacted] 25X1 part of the untied Eurodollar loans could be used to repay existing debts. [redacted]

OECD Inflationary Pressures Intensify

All of the major OECD countries except West Germany experienced higher inflation in consumer prices in first quarter 1974. Consumer prices are continuing to increase sharply in the second quarter as earlier rises in commodity prices are passed through to the final product and as large wage settlements remain common.

Increases in Consumer Prices[1]

	Percent Change at Annual Rate[2]	
	Fourth Quarter 1973	**First Quarter 1974**
Canada	6.8	11.2
France	10.4	16.8
Italy	13.6	25.2
Japan	20.0	34.0
United Kingdom	14.0	18.0
United States	8.8	13.2
West Germany	11.6	6.8

1. Based on OECD data.
2. Over the previous quarter.

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India: Improved Prospects for US Investment

India is taking another look at a previously rejected Dupont proposal to provide $3.3 million worth of technology in exchange for 40% equity in a new agricultural chemical plant and a previously ignored Burrough's proposal to invest about $80 million in the development of India's computer industry. An Indian Ministry of Commerce official has assured the US Embassy of the eventual approval of both proposals. New Delhi is loosening restrictions on private foreign investment, approving more proposals in the first three months of 1974 than in all of 1973.

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Canton Fair Business Dips Sharply

Overall assessment of the 1974 spring Canton Fair confirms the gloom expressed by many traders. Total business transacted at the fair was only about $800 million – down 40% from the 1973 fall fair. All the developed countries reported sharp declines from last fall. Contracts with Japan were down by one-third to $200 million and total US business of $17 million was off by more than half. Only the Third World countries appeared to have increased their business. Despite the poor results, China's trade boom is expected to continue in 1974 on the strength of contracts for Chinese goods from the fall fair, increased PRC petroleum exports, and deliveries of agricultural products and machinery from 1973 contracts.

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Publications of Interest

The Economic Situation in South Vietnam
(ER IR 74-13, May 1974, [redacted] 25X1

The May report on the South Vietnamese economy covers (1) the continued rise in prices, (2) the slight improvement in the foreign exchange position, (3) the poor prospects for the recovery of manufacturing output as a whole in spite of the growth of several import-substitute industries, and (4) trade and production problems caused by the global fertilizer shortage.

The Impact of Technological Transfer on the USSR
(OER-OCI Joint Publication, CIA No. 8113/74, June 1974,
[redacted] 25X1

This publication explores Soviet interest in technological transfer from the West and its likely economic and political impact on the USSR in a series of questions and answers. It deals with Soviet and US perceptions of the economic gains from detente, current Soviet foreign economic policy, the economics of detente, and the internal political alignments connected with detente. The publication then assesses the durability of current policies and the possible long-run effects on Soviet economic management and political control.

Estimating Military Hardware Production from Soviet Industrial Data
(ER RP 74-11, June 1974, [redacted] 25X1

This publication surveys Western attempts to estimate Soviet military hardware expenditures as residuals in official industrial data. It concludes that the estimates are unreliable because of ambiguities and gaps in the available data.

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INTERNAL ECONOMIC INDICATORS

GNP*
Constant Market Prices

	Latest Quarter	Percent Change from Previous Quarter	Average Annual Growth Rate Since 1970	1 Year Earlier	Previous Quarter
United States	74 I	-1.6	3.5	0.2	-6.3
Japan	73 IV	1.4	8.3	7.0	5.8
West Germany	73 IV	-0.1	3.1	3.4	-0.3
France	73 IV	1.8	5.8	5.7	7.3
United Kingdom	73 IV	-0.4	3.1	3.9	-1.4
Italy	73 I	0.8	3.1	5.2	3.4
Canada	73 IV	2.8	6.1	7.2	11.6*

WHOLESALE PRICES
Industrial

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Apr 74	2.4	8.6	20.8	[illegible]
Japan	Apr 74	0.7	11.2	35.6	22.9
West Germany	Mar 74	1.6	6.8	13.1	30.3
France	Apr 74	2.4	12.8	34.0	45.3
United Kingdom	Apr 74	3.3	10.7	23.9	45.2
Italy	Jan 74	7.1	11.8	33.9	68.3
Canada	Feb 74	1.5	9.7	19.8	27.8

INDUSTRIAL PRODUCTION*

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier**
United States	Apr 74	0.4	4.6	0.7	-6.2
Japan	Apr 74	-1.7	6.9	2.7	-9.9
West Germany	Mar 74	-1.7	3.2	1.1	-2.2
France	Mar 74	-0.8	6.4	5.0	5.4
United Kingdom	Mar 74	2.0	1.7	-4.0	-21.1
Italy	Mar 74	-2.4	3.9	11.0	-5.3
Canada	Feb 74	1.2	6.7	4.5	8.7

CONSUMER PRICES

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Apr 74	0.6	5.8	10.3	12.9
Japan	Mar 74	0.7	10.9	24.0	39.4
West Germany	Mar 74	0.3	6.2	7.2	7.7
France	Apr 74	1.6	7.7	13.2	17.7
United Kingdom	Apr 74	3.4	10.3	15.2	27.0
Italy	Apr 74	1.2	9.2	16.3	26.6
Canada	Apr 74	0.7	6.0	9.9	11.4

RETAIL SALES*
Current Prices

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier**
United States	Apr 74	1.4	10.6	8.3	10.8
Japan	Nov 73	3.4	14.6	27.4	32.0
West Germany	Feb 74	0.9	8.7	0.9	11.4
France	Feb 74	0.8	7.0	12.9	29.0
United Kingdom	Jan 74	-1.3	11.5	13.1	16.9
Italy	Oct 73	0.6	16.2	29.1	56.7
Canada	Mar 74	-1.0	11.4	11.8	23.1

MONEY SUPPLY*

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier**
United States	Apr 74	0.7	6.8	6.7	7.8
Japan	Jan 74	1.7	17.6	18.3	11.1
West Germany	Feb 74	0.5	8.8	1.1	8.6
France	Feb 74	-0.3	11.9	9.0	14.9
United Kingdom	Apr 74	2.7	9.3	3.0	1.0
Italy	Oct 73	1.6	20.7	23.0	21.4
Canada	Apr 74	4.2	13.8	14.4	18.5

MONEY-MARKET RATES

	Representative Rates	Latest Date	Percent Rate of Interest	1 Year Earlier	3 Months Earlier	1 Month Earlier
United States	Prime finance paper	31 May	9.25	6.75	7.25	9.00
Japan	Call money	3 Jun	12.50	6.63	12.00	12.00
West Germany	Interbank loans (3 Months)	31 May	9.38	14.00	10.50	9.50
France	Call money	28 May	13.00	7.63	12.75	11.75
United Kingdom	Local authority deposits	30 May	13.12	7.52	14.63	13.75
Canada	Finance paper	31 May	12.00	6.50	8.50	10.85
Euro-Dollars	Three-month deposits	31 May	11.88	8.69	8.88	11.50

*Seasonally adjusted.
**Average for latest 3 months compared with average for previous 3 months.

5 June 1974
Office of Economic Research/CIA

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EXTERNAL ECONOMIC INDICATORS

EXPORTS*
f.o.b.

	Latest Month	Million US $	Cumulative Million US $ 1974	1973	Percent Change
United States	Apr 74	8,230	30,624	20,908	46.5
Japan	Apr 74	4,207	15,293	10,941	39.3
West Germany	Apr 74	7,700	28,101	19,070	47.4
France	Apr 74	3,764	14,305	10,624	34.6
United Kingdom	Apr 74	3,112	10,814	8,801	22.9
Italy	Feb 74	2,095	4,081	3,063	32.6
Canada	Mar 74	2,029	7,530	5,991	25.7

EXPORT PRICES
US $

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Feb 74	3.5	11.0	27.6	38.3
Japan	Nov 73	-0.8	13.2	27.4	11.0
West Germany	Feb 74	7.1	12.5	23.9	5.6
France	Jan 74	5.9	11.1	18.9	35.2
United Kingdom	Dec 73	0.1	8.7	17.4	12.0
Italy	Oct 73	2.1	11.0	23.7	29.1
Canada	Jan 74	4.6	11.3	31.5	63.2

IMPORTS*
f.o.b.

	Latest Month	Million US $	Cumulative Million US $ 1974	1973	Percent Change
United States	Apr 74	8,138	29,843	21,545	38.5
Japan	Apr 74	4,076	16,634	8,785	89.3
West Germany	Apr 74	5,442	19,738	14,994	31.6
France	Apr 74	4,141	15,362	10,092	52.2
United Kingdom	Apr 74	4,066	14,655	9,796	49.6
Italy	Feb 74	2,847	5,017	3,298	52.1
Canada	Mar 74	2,077	7,410	5,541	33.7

EXPORT PRICES
National Currency

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Feb 74	3.5	11.0	27.6	38.3
Japan	Nov 73	3.6	4.8	14.9	34.1
West Germany	Feb 74	3.4	3.6	11.7	23.5
France	Jan 74	3.2	8.0	17.6	31.3
United Kingdom	Dec 73	3.1	9.8	18.8	33.0
Italy	Oct 73	2.4	8.3	20.4	17.0
Canada	Jan 74	3.7	9.0	30.5	56.7

TRADE BALANCE*
f.o.b./f.o.b.

	Latest Month	Million US $	Cumulative (Million US $) 1974	1973	Change
United States	Apr 74	92	781	-637	1,418
Japan	Apr 74	-409	-1,342	2,156	-3,498
West Germany	Apr 74	2,318	8,363	4,075	4,288
France	Apr 74	-377	-1,057	532	-1,589
United Kingdom	Apr 74	-954	-3,841	-995	-2,846
Italy	Feb 74	-752	-957	-235	-722
Canada	Mar 74	-48	120	450	-330

IMPORT PRICES
National Currency

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Feb 74	5.4	15.6	40.6	71.4
Japan	Nov 73	3.7	4.6	19.8	31.0
West Germany	Feb 74	3.5	5.9	22.7	75.7
France	Jan 74	14.9	11.3	33.0	127.4
United Kingdom	Dec 73	4.5	16.3	42.6	50.6
Italy	Oct 73	3.4	14.0	38.7	30.8
Canada	Jan 74	2.3	6.8	17.3	25.7

BASIC BALANCE**
Current and Long-Term Capital Transactions

	Latest Period	Million US $	Cumulative (Million US $) 1973	1972	Change
United States*	73 IV	214	1,209	-9,838	11,047
Japan	Apr 74	-1,005	-9,702	2,137	-11,839
West Germany	Mar 74	1,176	3,950	4,566	-616
France	73 IV	-352	-2,391	-369	-2,022
United Kingdom	73 IV	-1,394	-3,164	-1,989	-1,175
Italy	72 IV	800	N.A.	2,983	N.A.
Canada	73 IV	27	376	1,155	-779

EXCHANGE RATES Spot Rate
As of 31 May 74

	US $ Per Unit	Percent Change from Dec 66	18 Dec 1971	19 Mar 1973	24 May 1974
Japan (Yen)	0.0036	28.56	9.24	-6.73	-0.84
West Germany (Deutsche Mark)	0.3976	58.15	28.13	12.28	1.75
France (Franc)	0.2045	1.29	3.86	-7.21	0.63
United Kingdom (Pound Sterling)	2.3965	-14.12	-8.03	-2.62	0.15
Italy (Lira)	0.0016	-3.19	-9.88	-12.43	2.02
Canada (Dollar)	1.0402	12.77	4.25	4.26	0.09

OFFICIAL RESERVES

	Latest Month End of	Billion US $	Billion US $ Jun 1970	1 Year Earlier	3 Months Earlier
United States	Mar 74	14.6	16.3	14.0	14.4
Japan	Apr 74	12.7	4.1	16.8	11.6
West Germany	Mar 74	32.9	8.8	32.3	33.1
France	Apr 74	8.1	4.4	11.5	8.3
United Kingdom	Apr 74	7.0	2.8	6.1	6.2
Italy	Mar 74	6.7	4.7	6.3	6.4
Canada	Apr 74	6.2	4.3	6.1	5.9

TRADE-WEIGHTED EXCHANGE RATES***
As of 31 May 74

	Percent Change from Dec 66	18 Dec 1971	19 Mar 1973	24 May 1974
United States	-17.40	-8.00	-1.36	0.70
Japan	17.07	3.29	-8.62	-0.55
West Germany	33.49	16.36	11.31	-0.59
France	-22.15	-8.61	-11.05	0.78
United Kingdom	-34.04	-19.84	-5.46	0.78
Italy	-25.39	-24.02	-17.10	-0.94
Canada	9.35	2.74	4.38	0.11

*Seasonally adjusted.
**Converted into US dollars at current market rates of exchange.

***Weighting is based on each listed country's trade with 16 other industrialized countries to reflect the competitive impact of exchange-rate variations among the major currencies.

5 June 1974

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Annex to

Economic Intelligence Weekly

Japan: Well Into A Slump

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5 June 1974

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JAPAN: WELL INTO A SLUMP

1. The Japanese economy is experiencing its most pronounced slump since the 1950s. Industrial output has dropped sharply over the past six months, and real GNP probably declined a little in the first quarter. Economic growth for 1974 now seems likely to fall in the range of 2%-4% rather than the 3%-5% forecast a few months ago.

2. Tokyo's anti-inflation program has prolonged the downturn initiated by the pinch on oil supplies last winter. The most restrictive monetary and fiscal policies in years are curtailing domestic demand, while the economic slowdown abroad is restraining foreign demand for Japanese goods. Support for the Tanaka government nonetheless has held up well because unemployment remains low and inflation has eased slightly. Indeed, Tanaka's standing with the electorate is at its highest level of the past year.

3. The economy should begin a gradual recovery in the second half, its timing and strength depending heavily on Tokyo's policy decisions. Finance Minister Fukuda and other officials seem determined to throttle inflation even at further cost in economic growth. Since inflation seems to concern the Tanaka government more than maintaining output, we believe it will be very cautious in switching to expansionary measures. Although stimulative action is possible before the Diet elections in July, we doubt that it would be strong enough to raise real growth above 4% for the year.

The Slump Arrives

4. Japanese industrial output, on a seasonally adjusted basis, has slipped by 3.5% since February and 6% since November – the largest and most prolonged drop in 15 years. Though sharper than the declines in French, Canadian, US, and West German industry, the slide in Japan has not yet shaken confidence seriously. Only in a few industries, such as motor vehicles, has production fallen by 10% or more since November. Because of the large profits earned in late 1973, most firms have avoided financial problems despite weak sales and rising costs. Even the hardest-hit industries are maintaining employment by cutting working hours. The unemployment rate consequently is no higher now than a year ago – about 1.5% of the labor force.

5. In recent months, weak demand rather than inadequate oil supplies has been the main deterrent to economic growth. Consumer demand has fallen in real terms, as wages failed to keep pace with prices. At the same time, tight credit and slow sales have persuaded businessmen to postpone investment outlays. Other components of demand have not taken up much of the slack, as they did during

the 1971 downturn. Government spending has been declining in real terms, and the general slowdown in economic growth has eroded foreign demand for Japanese goods.

6. Japanese cost-of-living increases accelerated to annual rates averaging nearly 50% during the winter months. Production bottlenecks in certain industries, shortages of raw materials, speculative buying, and excess demand all played a part. Both the pinch on oil supplies and the huge rise in the cost of oil gave considerable impetus to price hikes. Initial efforts to curb aggregate demand were too moderate to help much. Not until the end of the year were monetary restraints tight enough to force postponement of investment outlays. Consumer demand remained strong through mid-February.

7. In addition to production constraints, Japanese industry experienced serious cost pressures in early 1974. Raw material costs had risen about 30% during the previous six months and increased further after oil prices were raised on 1 January. About half of the 10% increase in wholesale prices during the first quarter was due to rising prices for oil and other industrial materials. Higher labor costs also contributed to the price spiral. Because of the slump in industrial output, unit labor costs in January-February rose at an annual rate of 12%. By pushing up interest rates, the government's monetary policies raised business costs.

8. The rapid price rise early this year has induced Tokyo to maintain a tough anti-inflation program. Credit limits for small and medium-sized firms were relaxed in May to avoid a rash of bankruptcies. But the overall credit limit for April-June has been held close to that of the previous quarter, pushing interest rates to near-record levels. In March, the government placed price controls on 50 basic commodities and 150 important consumer items. These credit and price measures, together with weakening demand for some commodities, slowed the increase in consumer prices to an annual rate of 9% in March but the rate hit 38% in April.

9. Japan's economic downturn has aided the trade balance by dampening import demand and stimulating exports. Import volume during January-April 1974 was only slightly above year-earlier levels, while export volume rose an estimated 7% as Japanese firms boosted overseas sales to help offset sluggish demand at home. Even so, Japan had a trade deficit of $2.2 billion (not seasonally adjusted) in January-April 1974, compared with a $1.4 billion surplus in the same months of 1973. Deterioration in the balance was primarily the result of higher oil prices, which pushed the oil import bill from $1.6 billion in January-April 1973 to $5.5 billion this year. To protect foreign reserves, Tokyo has reduced long-term capital outflows and encouraged borrowing abroad.

A Turnaround in the Second Half

10. Japanese economic activity should turn up in the second half and generate a moderate gain in GNP for the year as a whole. Finance Minister Fukuda wants

to restrain demand firmly until the fall, hoping to bring inflation under control by then. We believe that postponing stimulative action until that time would hold the gain in GNP to 2% this year. Unless industrial output recovers in the months ahead, pressures to ease policies sooner will be hard to resist. If Tokyo stimulates demand within the next couple of months, economic growth probably could reach 4% in 1974, still far below the 10% average of the last decade.

11. Since the short-term outlook is for sluggish output and higher prices, it is difficult to judge what the government will do. The slump in output gradually has spread to light industry, which generally lacks the financial resources of heavy industry. Output in heavy industry also threatens to slip further, now that inventories of finished goods are beginning to exceed normal levels. Tight money continues to hurt the construction industry. The value of construction orders picked up substantially in March, but in real terms they probably are still running below year-earlier levels.

12. Even if Tokyo stimulates demand soon, recovery will be gradual. New orders for machinery and equipment plummeted during the first three months of 1974, and surveys suggest continuing weakness in fixed investment until the fourth quarter. A substantial slowdown in inventory accumulation appears likely, following the near-record increase during the past six months. The impact on personal spending of the 30% wage hikes won by most workers in April will be partly offset by a desire to rebuild savings. During the early months of 1974, Japanese households reduced their savings rate well below normal in an effort to maintain living standards in spite of soaring prices and reduced overtime pay.

Strong Wage-Push Coming for Prices

13. Although the worst of the price spiral appears over, rapid inflation in the months ahead seems assured because industry will face severe cost pressures. Higher labor costs stemming from the record 1974 wage hikes will be the chief factor sustaining inflation. With industrial output likely to stagnate during the next few months, productivity gains will be too small to prevent substantial increases in unit labor costs. When price controls are lifted in the months ahead industry also will move to pass along higher production costs stemming from increased prices for oil and other raw materials. Given the magnitude of the wage and price hikes facing industry, Tokyo's objective of forcing firms to absorb a large portion of the cost increases seems unrealistic.

Balance of Payments Under Control

14. Tokyo's hopes of achieving a trade surplus this year are fading. Although the expected moderate drop in Japanese import volume should help bring commodity prices down, several months will pass before declines show up in the trade account. The import bill in 1974 is expected to expand about 60% to $52 billion, with oil costs accounting for roughly two-thirds of the rise. As a result of sharply increased prices and moderate volume gains, Japan's export earnings

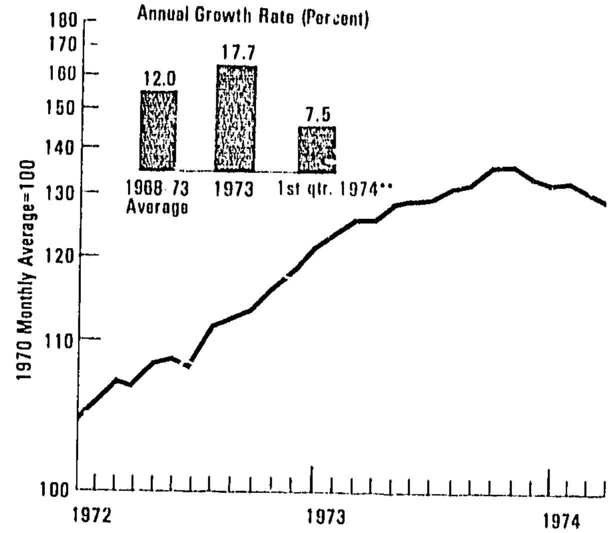
are growing at a record rate of 40%. Even if this pace is maintained throughout the year, Japan will still register an overall 1974 trade deficit of about $2 billion compared with a $3.7 billion surplus in 1973. Japan has a strong chance, however, of restoring trade surpluses toward the end of this year.

15. With the trade account $2 billion in the red, Japan can expect a current account deficit of about $7 billion and a deficit in the basic balance of around $10 billion. Tokyo probably will be unable or unwilling to hold long-term capital outflows to less than $3 billion compared with last year's $10 billion level. Substantial loan and investment commitments have already been incurred, and Tokyo is determined to make funds available to help develop raw material resources abroad.

16. Despite the expected large deficit in the basic balance, Tokyo should be able to maintain official reserves near their current level of $12 billion to $13 billion. This can be accomplished by drawing on non-official holdings of foreign exchange and by borrowing short-term funds abroad. Non-official holdings -- mostly dollar deposits in Japanese commercial banks -- still amount to almost $8 billion. The Japanese already have increased their short-term borrowing abroad by some $5.5 billion, much of it in the United States, and they can borrow more if necessary. Tokyo clearly considers such moves only as temporary expedients. In the longer term, it will be aiming at least for balance in the current account, which will require returning to sizable trade surpluses.

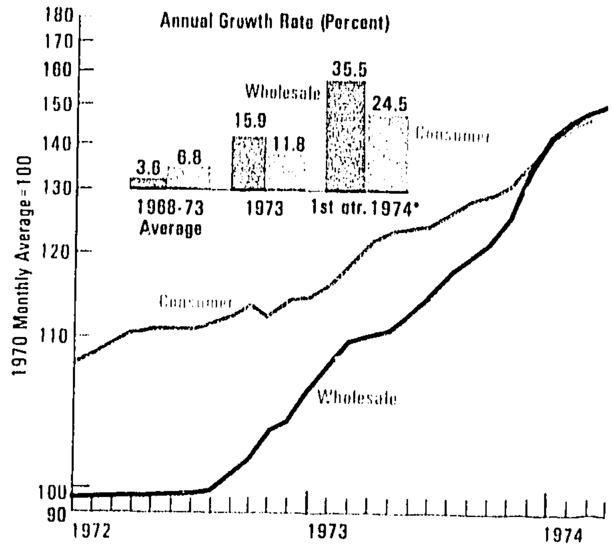
JAPAN: INTERNAL ECONOMIC INDICATORS

INDUSTRIAL PRODUCTION*



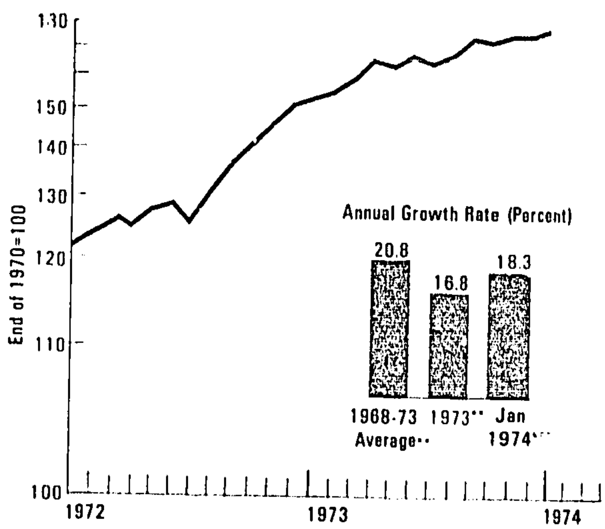
*Seasonally Adjusted.
**Increase over comparable period of 1973.

PRICES



*Increase over comparable period of 1973.

MONEY SUPPLY*



*Seasonally Adjusted.
**Based on end of year data.
***Increase over comparable period of 1973.

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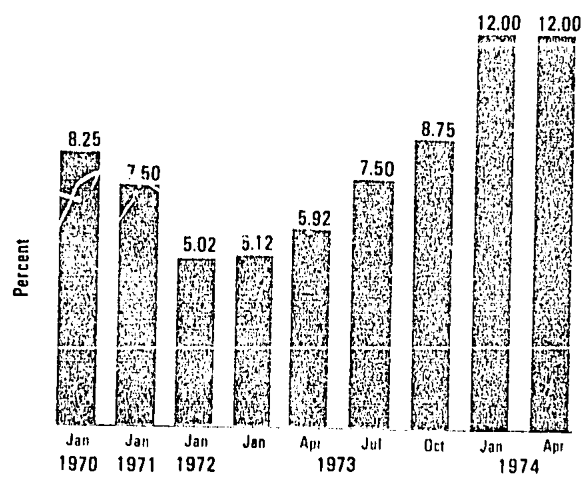
MONEY MARKET RATES

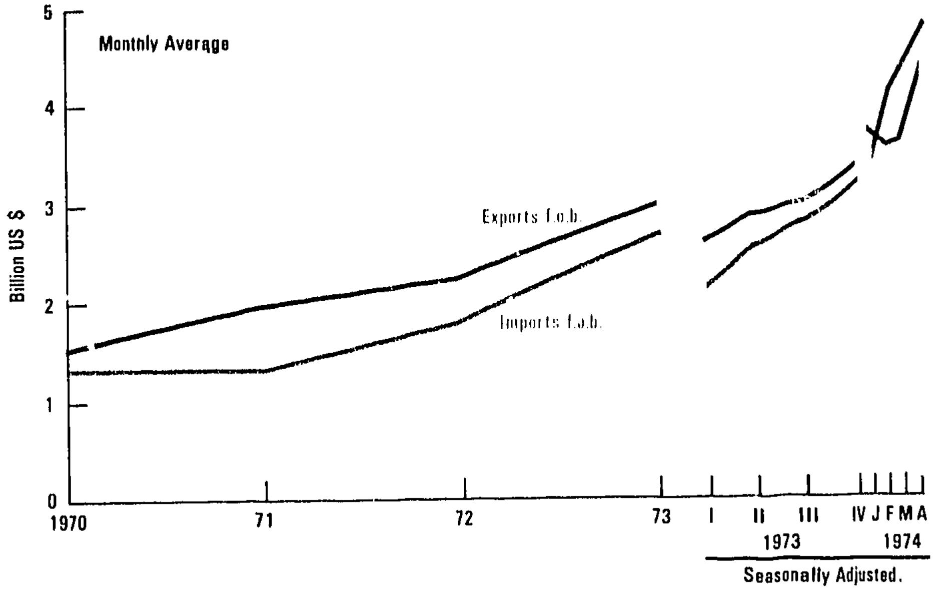
Interest Rate for Call Money



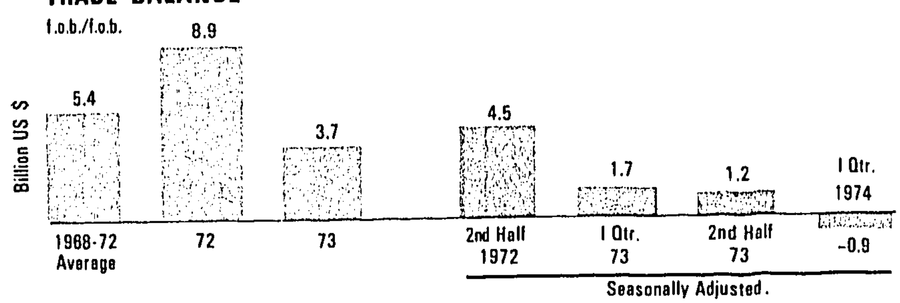
Note: End of period.

JAPAN: EXTERNAL ECONOMIC INDICATORS

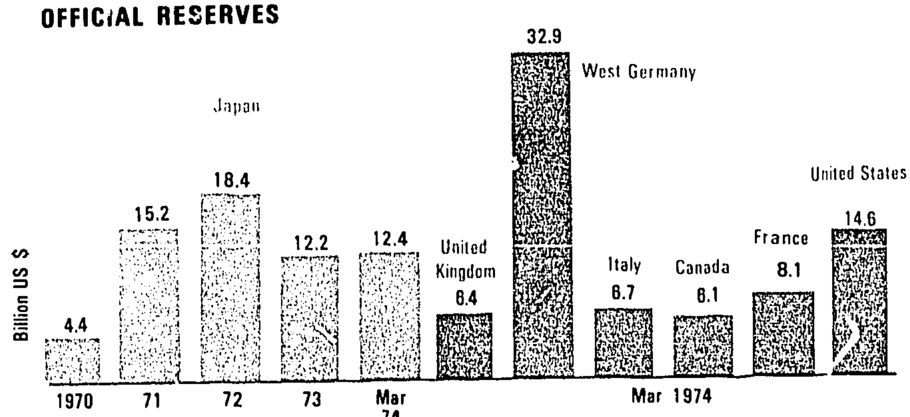
VALUE OF TRADE



TRADE BALANCE



OFFICIAL RESERVES



Note: End of Period.

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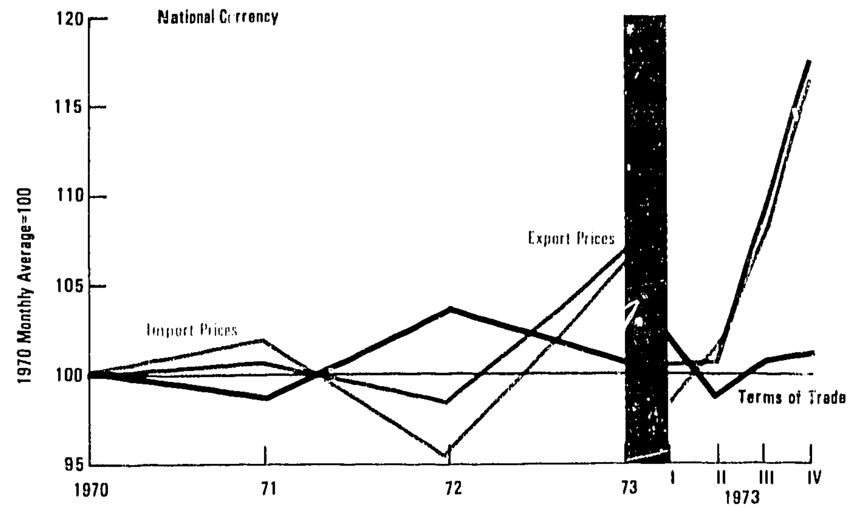
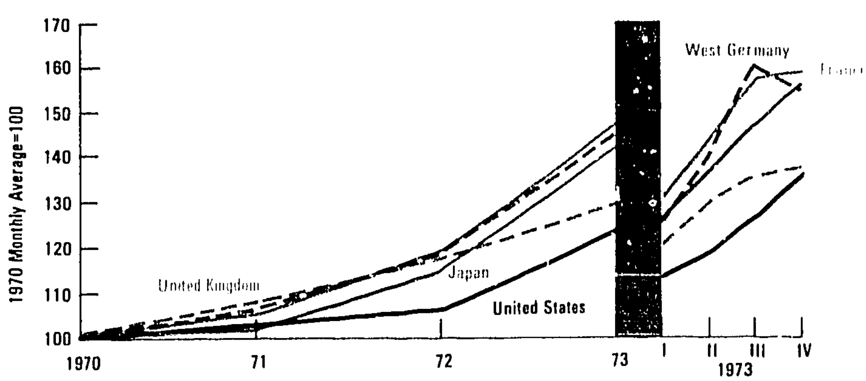
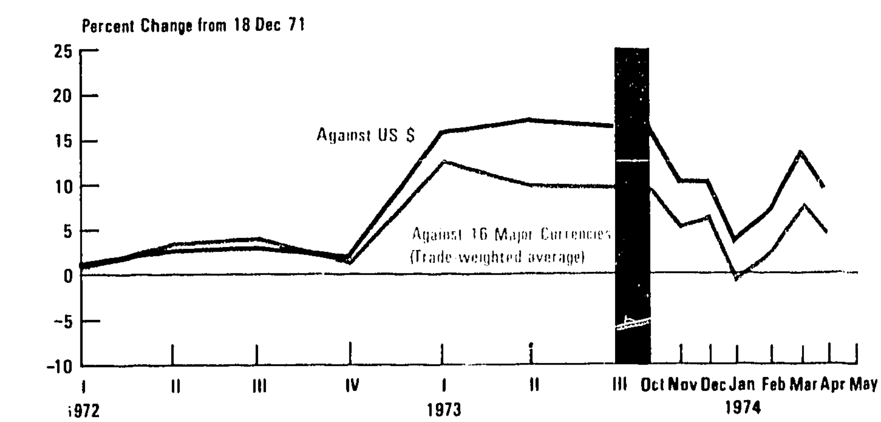
TERMS OF TRADE



EXPORT PRICES IN US $



EXCHANGE RATES FOR THE YEN



Note: End of Period.